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SUBJECT: MANGYSTAU - KAZAKHSTAN'S OTHER OIL CENTER

REF: ASTANA 01865

¶1. (U) Sensitive but unclassified. Not for public Internet.

¶2. (SBU) SUMMARY: On November 6, DCM and poloff met with several oil companies to discuss the state of the energy industry in Kazakhstan's Mangystau oblast. Oil companies in Mangystau noted the region's untapped potential, good infrastructure, a supportive local government, and well-qualified work force as reasons for their success. Companies also reiterated the need to develop the region's environment and social services. END SUMMARY.

REGIONAL COMPARATIVE ADVANTAGES: MODERN INFRASTRUCTURE AND SUPPORTIVE LOCAL GOVERNMENT

¶3. (SBU) On November 5, Poloff and DCM met with the General Director of Caspiy Meruerty Operating Company BV, a 50-person operating company and subsidiary of Shell and Oman Pearls. The company made a strategic decision to establish itself in Mangystau province, rather than Atyrau, where most Western companies are based. Caspiy Meruerty's General Director, Marcus Antonini, told DCM and poloff that the decision has worked out well for the company, due to its access to Mangystau's relatively untapped reserves. (NOTE: Caspiy Meruerty struck oil last month on two test wells. END NOTE.)

Caspiy officials also said that Mangystau has better infrastructure than Atyrau, in particular, better port facilities and a very accommodating local government. Antonini noted that joint ventures are very important to the region, and the Akim (governor) is ambitious, and, in a good sense, nationalistic.<sup>8</sup> Caspiy has had no problems getting work permits or other paperwork approved. Antonini also stated that the capital city of Mangystau, Aktau, is also a more attractive city than Atyrau, an important factor in attracting foreign investment.

¶4. (SBU) FMC Technologies representative Tanat Ishangali echoed Antonini's comments and said that the business climate in Mangystau is excellent. FMC has two major customers in the oblast, Agip and Myers, and competes on quality, not price. Ishangali, whose brother works in a Chinese firm, claims that FMC's Chinese competitors manufacture oil pumping equipment that is five times less

expensive, but made of soft metal and prone to leaks. To meet local content requirements, FMC purchases parts from Kazakhstan, then makes the casing spool bodies at a factory in France and completes welding in Almaty. Ishangali declared that FMC, which employs 51 people in Aktau, also has had no problems processing work permits in Mangystau.

#### MANGYSTAU HAS PLENTY OF WELL-QUALIFIED WORKERS

¶ 15. (SBU) Caspiy Meruerty, s Antonini also said that the Mangystau region has plenty of well-qualified workers, noting that he has hired 40 people over the last year. Many of Caspiy Meruerty, s new employees have previous experience in the oil service industry and oil well work, having worked at other international oil companies such as Schlumberger, Baker-Hughes and Agip. Antonini commented that Shell has also noticed a trend of Kazakhstani citizens overseas returning to Kazakhstan to work, despite the fact that many will lose the tax-free status they enjoyed when employed outside their home country.

#### REGION HAS POTENTIAL UNDER VARIOUS TRANSPORTATION SYSTEMS

¶ 16. (SBU) Antonini told poloff that there is huge growth potential in Mangystau, particularly in the four fields located 20 kilometers offshore. Antonini reminded DCM and poloff that, as an operator, he is less concerned with transportation issues. Whether oil is exported via the Kazakhstan Caspian Transportation System (KCTS) or the Caspian Pipeline Consortium (CPC) pipeline, Antonini sees significant growth opportunities. In particular, Antonini noted that domestic refining capacity in Kazakhstan is limited and therefore Kazakhstan imports the majority of its refined products. If Kazakhstan had increased refining capacity, this would present domestic business opportunities for a number of companies. (COMMENT: Kazakhstan has been considering how to address its under-investment in refining capacity, per reftel. END COMMENT.) In Antonini, s view, future cooperation with Iran remains difficult due to the political situation. Nevertheless, Antonini said that Total has studied plans to build a pipeline from Kazakhstan to Iran and called this potentially & a brilliant investment<sup>8</sup> that could have a big pay-off someday. (COMMENT: Poloff could not independently confirm this report, which goes beyond statements made by international oil companies operating in Kazakhstan. END COMMENT.) A pipeline south to India and Pakistan would be ideal, too, he said, if the situation in Afghanistan were secure enough to make it worthwhile. Antonini also commented that the most interesting aspect of the Kazakhstan International Oil and Gas Exhibition in Almaty this year was the lack of a Chinese presence, considering the joint project to build an oil pipeline from the Caspian Sea to China.

#### ENVIRONMENTAL PROTECTION AND SOCIAL INFRASTRUCTURE NOT YET ADEQUATE

¶ 17. (SBU) As part of their Production Sharing Agreements, oil companies are required to invest in projects to develop the local social infrastructure, and investing in Astana or Almaty is forbidden. Antonini notes that initially, Caspiy Meruerty invested primarily in small projects, such as public lavatories and playgrounds. This year, however, several companies combined their investments to construct a kindergarten and a water pipeline to a nearby town. Although Antonini stated that environmental restrictions, such as the zero discharge policy, are strict and discourage testing of wells, his company was able to work successfully within such environmental protection constraints. Caspiy Meruerty used special equipment, including burners from Venezuela, to run an emission-free test. Waste disposal and processing, and other quality-of-life issues, however, are critical to Mangystau, s future. According to Antonini, the region could do more to clean up the beaches and develop its recreational potential. Antonini also noted his concern that regional education and health-care systems have been placed too much &on the back burner.<sup>8</sup> Antonini commented that from the very large number of border guards patrolling the Caspian

Sea, illegal fishing is clearly a large problem, and he said the illegal nets create a hassle for off-shore oil companies such as Caspiy Meruerty.

#### LOCAL PARTNERSHIPS ARE KEY

¶8. (SBU) Antonini told DCM and poloff that he believes that Caspiy Meruerty has succeeded because the company carefully studied every other foreign company in Kazakhstan to see what difficulties they encountered and tried to avoid these challenges. Noting that many foreign enterprises were caught off guard by subsoil legislation changes, Antonini commented that companies have to be realistic and proactively engage government partners. For instance, in its second round of tenders, Caspiy Meruerty leveraged the local government's extensive experience to help select good candidates.

Antonini remarked that he looks for long-term partnership with local Kazakhstani enterprises, particularly with companies that have decent equipment, sufficient capital, and a broad, flexible outlook. (COMMENT: Currently, Aktau is clearly number two behind Atyrau as a Caspian oil center. However, many of the offshore fields are equidistant between Aktau and Atyrau, and a number of Western companies feel that the local administration (oblast) in Atyrau has become difficult and greedy. Aktau, on the other hand, seems more business-friendly and is certainly trying harder to welcome investment at this point. END COMMENT.)

HOAGLAND